89- 1542

No. _____

In The

Supreme Court of the United States

October Term, 1989

BIZCAP, INC.,

Petitioner,

v.

ANTHONY P. OLIVE, Director of Virgin Islands Bureau of Internal Revenue, and GOVERNMENT OF THE VIRGIN ISLANDS,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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QUESTION PRESENTED

Should a statute that defines rights and obligations by reference to pre-existing legal rules be presumed to require application of those rules as they were understood by Congress at the time of enactment of the new statute, without regard to post-enactment judicial interpretation of the prior law?

PARTIES TO THE PROCEEDING

Petitioner states that the following parties appeared in the U.S. Court of Appeals for the Third Circuit:

The Government of the Virgin Islands

Anthony Olive: appearing in his official capacity as Director of the Virgin Islands Bureau of Internal Revenue

Bizcap, Inc. (now known as Caribbean Marine, Inc.): a corporation with a publicly traded affiliate known as 50-Off Stores, Inc.

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Petitioner, Bizcap, Inc., respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Third Circuit entered in this proceeding on December 29, 1989. A petition for rehearing was denied on January 30, 1990.

OPINIONS BELOW

The opinion and order of the United States District Court for the Virgin Islands (unreported) is reproduced in Appendix B. The opinion of the United States Court of Appeals for the Third Circuit is reported at 892 F.2d 1163 and is reproduced in Appendix A. No opinion was issued on denial of petition for rehearing.

JURISDICTION

The judgment of the Court of Appeals was entered on December 29, 1989, and a timely petition for rehearing was denied on January 30, 1990. This petition is filed within sixty days of entry of the order denying the petition for rehearing. This Court's jurisdiction is invoked pursuant to 28 U.S.C. Section 1254(1).

STATUTORY PROVISIONS INVOLVED

1. The Naval Appropriations Act of 1921, 48 U.S.C. § 1397;

2. Revised Organic Act of 1954, 48 U.S.C. § 1642;

3. The Tax Reform Act of 1986, Sections 1275(b) and 1277(c)(2) (Internal Revenue Code Section 7651(5)(B) and Note to Section 931; 26 U.S.C. § 7651(5)(B) and Note to 26 U.S.C. § 931).

STATEMENT OF THE CASE

A. Summary of the Issue Presented

When Congress enacts a statute, the pre-existing framework of legal rules, including judicial interpretations of prior law, is an important element of context for understanding the new enactment. Indeed, in many cases, the explicit motivation for the new statute is to change one or more of those prior judicial interpretations.

This case poses a recurring constructional problem that arises when Congress defines a party's rights and obligations in terms of the application of pre-existing legal rules, and those rules are given a different judicial interpretation *subsequent* to enactment of the new statute.

Specifically, in 1986 a district court decision exposed (or, if one prefers, created) a tax loophole for certain corporations doing business in the Virgin Islands. Shortly thereafter, Congress closed the loophole by enacting section 1275(b) of the Tax Reform Act of 1986, Pub. L. No. 99-514, 100 Stat. 2598, (codified at 26 U.S.C. § 7651(5)(B). However, section 1277(c)(2)(D) of the Act, Pub. L. No. 99-514, 100 Stat. 2601, (codified as a Note to 26 U.S.C. § 931) carved out an exemption from some of section 1275(b)'s loophole-closing effects for two companies, including Petitioner. The form of the exemption was to give Petitioner the benefit of the pre-Tax Reform Act law. The District Court decision that Congress overruled in 1986 by its legislative action was later reversed by the Third Circuit Court of Appeals in 1987. That interpretation of pre-Tax Reform Act law was followed by the Third Circuit in the present case, and we (grudgingly) accept it here.

The question raised by this petition is whether section 1277(c)(2)(D) should be presumed to have incorporated the well understood judicial interpretation of prior law extant at the time of its enactment in 1986, or whether Petitioner's rights were properly deemed to be contingent on subsequent judicial developments.

B. The Factual and Legal Background

Petitioner Bizcap, Inc. ("Bizcap")[1] is a Delaware corporation and an inhabitant of the Virgin Islands. While it actively conducts business in the Virgin Islands, much of its income results from passive investments made in the mainland United States. Petitioner's hybrid status – as both a foreign corporation in and an inhabitant of the Virgin Islands[2] – and its multiple sources of income gave rise to the present dispute.

While this petition seeks review only of the Third Circuit Court of Appeals' construction of section

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[1] At the time of the events giving rise to this suit, Petitioner was called Bizcap, Inc. but has been known as Caribbean Marine, Inc. since 1987. The District Court referred to Petitioner as "CMI" and the Third Circuit Court of Appeals referred to Petitioner as "Bizcap".

[2] These are different concepts. A corporation's status as foreign or domestic is determined by its place of incorporation; Petitioner, for example, was incorporated in Delaware and is thus deemed to be "foreign" when doing business in the Virgin Islands. An "inhabitant" of the Virgin Islands, by contrast, is any "person[ ] whose permanent address is in the Virgin Islands," 48 U.S.C. § 1642 (Supp. V 1987), which (it is conceded by all) includes Petitioner. *See* Pet. App. at A-3.

1277(c)(2)(D) of the Tax Reform Act of 1986, a brief discussion of the broader interplay between the federal and Virgin Islands tax laws is necessary to a full understanding of that issue – and of the broader question of statutory interpretation that it illustrates. Ever since the Naval Appropriations Act of 1921, ch. 44, 1, 42 Stat. 123 (codified as amended at 48 U.S.C. § 1397 (Supp. V 1987)), taxation in the Virgin Islands has been governed by the so-called "mirror" tax system. Under that system, the federal tax laws – today meaning the Internal Revenue Code – are declared also to constitute the tax laws of the Virgin Islands, with the words "Virgin Islands" substituted for the words "United States" wherever appropriate, and with any taxes due under the mirrored Virgin Islands tax code payable directly into the Virgin Islands treasury. *See* Pet. App. A-4-5, *Danbury, Inc. v. Olive*, 820 F.2d 618, 620-21 (3d Cir. 1987), *cert. denied*, 484 U.S. 964 (1987) (hereinafter referred to as *"Danbury II"*). For example, the Virgin Islands tax liability of foreign corporations that are inhabitants of the Virgin Islands is determined under the mirror system by reference to I.R.C. 882(b) (1982), which (substituting the words "Virgin Islands" for "United States") limits the relevant gross income of such a corporation to

> (1) gross income which is derived from sources within the Virgin Islands and which is not effectively connected with the conduct of a trade or business within the Virgin Islands and
> (2) gross income which is effectively connected with the conduct of a trade or business within the Virgin Islands.

I.R.C. 882(b) (1982). In other words, considering the mirror system in isolation, a Delaware corporation doing

business in the Virgin Islands is treated for Virgin Islands tax purposes exactly like a French corporation doing business in the United States is treated for federal tax purposes.

As originally implemented,[3] this mirror system required domestic United States corporations doing business in the Virgin Islands to file two tax returns: one with the Virgin Islands Bureau of Internal Revenue ("BIR")[4] covering income included within the mirrored version of I.R.C. 882(b), and one with the federal Internal Revenue Service covering worldwide income (with allowance of a foreign tax credit for any taxes paid to the BIR). The administration of this system was changed in 1954 by section 28(a) of the Revised Organic Act of the Virgin Islands, ch. 558, 28(a), 68 Stat. 508 (1954) (codified as amended at 48 U.S.C. § 1642 (Supp. V 1987)), which permits all "inhabitants" of the Virgin Islands to "satisfy their income tax obligations under the applicable taxing statutes of the United States by paying their tax on income derived from all sources both within and outside the Virgin Islands into the treasury of the Virgin Islands . . . "[5] Section 28(a), sometimes referred to as the

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[3] The mirror system was not actually implemented according to its statutorily required terms until 1935. *See Danbury II*, 820 F.2d at 621.

[4] The Virgin Islands Bureau of Internal Revenue together with its Director, Anthony P. Olive, and the Government of the Virgin Islands are collectively referred to as the "BIR".

[5] 48 U.S.C. § 1642 (Supp. V 1987). The relevant portion of the statute provides in full:

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"inhabitant rule," thus enabled foreign inhabitants to take care of both federal and Virgin Islands tax obligations in a single filing and payment.

However, the subsequent 1954 codification of the federal tax laws into the Internal Revenue Code threatened to undo this administrative improvement. Because "[t]he language of the Internal Revenue Code . . . speaks in terms of all United States taxpayers owing their United States taxes to the Internal Revenue Service," *Danbury II*, 820 F.2d at 623, the Code's enactment could have been viewed as superseding section 28(a)'s authorization to pay United States taxes directly to the Virgin Islands. Thus, when Congress enacted the Internal Revenue Code in 1954, it included a provision declaring that "[f]or purposes of this title . . . section 28(a) of the Revised Organic Act of the Virgin Islands shall be effective as if such

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> The proceeds of customs duties, the proceeds of the United States income tax, the proceeds of any taxes levied by the Congress on the inhabitants of the Virgin Islands, and the proceeds of all quarantine, passport, immigration, and naturalization fees collected in the Virgin Islands . . . shall be covered into the treasury of the Virgin Islands, and shall be available for expenditure as the Legislature of the Virgin Islands may provide: *Provided*, That the term "inhabitants of the Virgin Islands" as used in this section shall include all persons whose permanent residence is in the Virgin Islands, and such persons shall satisfy their income tax obligations under the applicable taxing statutes of the United States by paying their tax on income derived from all sources both within and outside the Virgin Islands into the treasury of the Virgin Islands. . . .

section had been enacted *subsequent* to the enactment of this title." 26 U.S.C. § 7651(5)(B) (1982) (emphasis added). This made section 28(a)'s administrative innovation an amendment of the Code rather than vice versa, thus assuring its effectiveness.

It also gave rise three decades later to a court decision involving another foreign corporate inhabitant of the Virgin Islands, in which the statutes set forth above were construed to create, in the court's own language, "the ultimate tax shelter". *Danbury, Inc. v. Olive*, 627 F. Supp. 513, 518 (D. V.I. 1986) (hereinafter referred to as "*Danbury I*"), *rev'd*, 820 F.2d 618 (3d Cir. 1987) *cert. denied*, 484 U.S. 964 (1987). The District Court in *Danbury I* reasoned as follows: (1) The mirrored version of I.R.C. 882(b) requires inhabitant foreign corporations in the Virgin Islands to pay Virgin Islands tax only on income from Virgin Islands sources or from a trade or business carried on in the Virgin Islands; the passive receipt of income from investments outside the Virgin Islands falls into neither category. (2) Section 28(a) permits Virgin Islands inhabitants to satisfy both their United States and their Virgin Islands tax obligations by paying their Virgin Islands tax, if any, on all sources of income to the BIR. Therefore, (3) inhabitant foreign corporations in the Virgin Islands who derive income from passive investments made outside the Virgin Islands owe no tax at all on that income. *See Danbury I*, 627 F. Supp. at 516-19.

Petitioner Bizcap was among the many corporations cheered by this result, as several years earlier it had reached the same conclusion as the District Court. Although Petitioner conducts extensive business in the Virgin Islands, the income from which is clearly taxable by

the BIR, it also has substantial income that falls outside the terms of the mirrored I.R.C. 882(b). Petitioner listed over $16.6 million in non-Virgin Islands source income on its 1983 and 1984 Virgin Islands returns, which it claimed were subject to no tax. *See* Pet. App. A-3. The BIR disagreed with petitioner's reading of the law, and on November 7, 1985, it issued a notice to Petitioner alleging deficiencies and penalties for the 1983 and 1984 tax years totalling almost $5.9 million. *See* Pet. App. A-4. Petitioner sought a redetermination of that liability in the Virgin Islands District Court. *See* Pet. App. A-4.

Congress, needless to say, moved swiftly to close the loophole exposed by *Danbury I*. Section 1275(b) of the Tax Reform Act of 1986 amended I.R.C. 7651(5)(B) to provide that section 28(a) – the Virgin Islands inhabitant rule – shall be effective "as if such section 28(a) had been enacted *before* the enactment of this title and such section 28(a) shall have no effect on the amount of income tax liability required to be paid by any person to the United States." I.R.C. 7651(5)(B) (emphasis added). The amendment thus returned the Virgin Islands tax system "to the pre-1954 system where a foreign corporation doing business in the Virgin Islands must file two returns," Pet. App. A-7, and pulled the plug on the *Danbury I* decision. The change covers all tax years "beginning after December 31, 1986," Tax Reform Act of 1986, § 1277(c)(2)(A)(i), Pub. L. No. 99-514, 100 Stat. 2601, (codified as a Note to 26 U.S.C. § 931), and was generally made retroactive to all pre-1987 "open years" – that is, years for which a deficiency assessment would not be barred by any applicable statute of limitations. *See Id.* at § 1277(c)(2)(A)(ii) & § 1277(c)(2)(C).

However, as the result of a hard-fought Bizcap lobbying effort vigorously opposed by the BIR, Petitioner secured for itself an exemption from the *retroactive* application of the loophole-closing provisions of the Tax Reform Act. Section 1277(c)(2)(D) of the Act – the statute specifically at issue in this case – provides in full:

> (D) Exception. – In the case of any pre-1987 open year, the amendment made by section 1275(b) shall not apply to any domestic corporation if –
>
> (i) during the fiscal year which ended May 31, 1986, such corporation was actively engaged directly or through a subsidiary in the conduct of a trade or business in the Virgin Islands and such trade or business consists of business related to marine activities, and
>
> (ii) such corporation was incorporated on March 31, 1983, in Delaware.

Pub. L. No. 99-514, 100 Stat. 2601, (codified as a Note to 26 U.S.C. § 931). Not at all coincidentally, Petitioner precisely fits this description.

C. The Proceedings Below

On June 5, 1987, more than six months after passage of the Tax Reform Act, the Third Circuit issued its decision in *Danbury II*, holding that section 1275(b) of the Tax Reform Act, if applicable to the tax years at issue in that case, closed the loophole for Danbury (who plainly did not fit within section 1277(c)(2)(D)'s targeted exemption) and remanding for a determination of the statute's applicability. *See Danbury II*, 820 F.2d at 625-28. However, in dicta, the Court of Appeals also took issue with the District Court's interpretation of the pre-Tax Reform Act

law, suggesting that Congress had acted in 1986 to close a loophole that never existed in the first place. *See id.* at 622-25.[6]

Subsequently, the District Court in this case granted Petitioner's motion for summary judgment on the ground that the targeted exemption in section 1277(c)(2)(D) of the Tax Reform Act assured Petitioner of immunity from tax liability for the relevant years. Pet. App. B-2 and 8. The Court of Appeals for the Third Circuit reversed. It agreed (as did the BIR) that section 1277(c)(2)(D) exempted Petitioner from the retroactive loophole-closing effects of the Tax Reform Act, but held, on the strength of the dicta in *Danbury II*, that there was in fact no loophole to close.[7]

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[6] In particular, the Court of Appeals took issue with the District Court's interpretation of section 28(a). Since we assume for purposes of this petition that the Court of Appeals was correct in this regard, *see infra* note 7, the details of its analysis are not relevant.

[7] *See* Pet. App. A-10 (citation omitted):

> At the time the Act was passed, Congress believed the interplay between 26 U.S.C. §§ 882 and 28(a) resulted in a tax loophole. Bizcap lobbied to have the loophole applied to it by avoiding the retroactive effect of the repeal of the inhabitant rule. However, since we determined in *Danbury* that there was no loophole, the exception granted to Bizcap results in Bizcap remaining liable to the BIR for taxes on both its stateside and Virgin Islands source income for 1983 and 1984.

The Court of Appeals viewed *Danbury II* as binding precedent on the state of pre-1987 (*i.e.*, pre-Tax Reform Act) law. *See* Pet. App. A-11. While this view represents a patent misinterpretation of *Danbury II*, its result is a square holding in the present

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Pet. App. A-10-11. The result was to place Petitioner in exactly the same position as companies that did not benefit from section 1277(c)(2)(D)'s targeted exemption. The Court of Appeals thought that this result followed from the plain language of section 1277(c)(2)(D), which "only exempts Bizcap from the retroactive effect of the tax law change [effected by section 1275(b)]. Thus, Bizcap remained liable under the previous tax laws applicable to the Virgin Islands, *whatever they were or were determined to be by our court* in *Danbury*." Pet. App. A-10 (emphasis added). Petitioner was, argued the Court,

> fully aware that the *Danbury* decision had been appealed to us and that the decision could be reversed. Rather than couch the exception in terms of the retroactivity of the repeal of the inhabitant rule, the drafters of the legislation could have specifically stated that the targeted corporations were exempt from tax liability on stateside income for the years in question. However, that is not what happened here. Instead, Congress chose clear language which linked Bizcap's exception to the application of the Virgin Islands law prior to the repeal of the inhabitant rule.

Pet. App. A-10.

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case that pre-1987 law did not provide the tax shelter relied on by Petitioner and others. We believe that this holding is erroneous on its merits, but we do not seek certiorari on this aspect of the Court of Appeals' decision. Thus, for purposes of this petition, we assume that the District Court in *Danbury I* miscontrued the pre-1987 law.

Chief Judge Gibbons dissented, concluding that the majority's analysis "distorts the plain language of section 1277(c)(2)(D)," Pet. App. A-15, and attributes to Congress an "unlikely" intention. Pet. App. A-15. According to Chief Judge Gibbons,

> The majority implies that Congress intended to make the effect of the statute depend on our subsequent determination in *Danbury* of the scope of section 1275(b) and the inhabitant rule. That analysis suggests that . . . the statute's purpose was merely to make Bizcap's fortunes depend on Danbury's success in the Court of Appeals, as we later construed another statute, in litigation in which Bizcap was unrepresented. That is, the majority would now have us believe that the purpose of Congress evident on the face of section 1277(c)(2)(D) was not to hand Bizcap a victory, nor even to hand the BIR a victory, but to give Bizcap a sporting chance of victory in the *Danbury* court. This logically awkward conclusion strains credulity.

Pet. App. A-16.

REASON FOR GRANTING THE WRIT

THIS CASE PRESENTS AN IMPORTANT AND RECURRING QUESTION OF WHETHER A STATUTE THAT DEFINES RIGHTS AND OBLIGATIONS BY REFERENCE TO PRE-EXISTING LEGAL RULES SHOULD BE PRESUMED TO REQUIRE APPLICATION OF THOSE RULES AS THEY WERE UNDERSTOOD BY CONGRESS AT THE TIME OF ENACTMENT OF THE NEW STATUTE AND WITHOUT REGARD TO POST-ENACTMENT JUDICIAL INTERPRETATION OF THE PRIOR LAW.

The panel's disagreement over the meaning of section 1277(c)(2)(D) is significant. The statute admits of

different constructions, depending upon the presumptions brought to bear upon it. Although this Court has on several occasions been faced with somewhat analogous situations, it has never clearly set forth the appropriate rule of construction. We ask it to do so now.

A. A Presumption that Prior Law Should Be Applied as it Stood at the Time of Enactment of Section 1277(c)(2)(D) is Justified

All statutes are enacted in light of assumptions about such matters as the meaning of words, the character of social institutions, and the pre-existing legal framework. Assumptions about the legal framework in particular become critical when statutes, as they often do, define rights and obligations indirectly by reference to the application of prior law rather than directly through detailed specification of the parties' entitlements. This case starkly illustrates the interpretative problems that such statutes can pose.

As the Third Circuit majority correctly observed, section 1277(c)(2)(D) does not state precisely, "Bizcap is not liable for any tax for the relevant years." Instead, the section says, in essence, "For open years before 1987, Bizcap, unlike other taxpayers, should have its tax liability determined without reference to the rest of the Tax Reform Act." The Court of Appeals, however, failed to recognize that this merely states the issue; it does not resolve it. One perhaps could construe the statute, as did the majority, to consign Petitioner to pre-1987 law *however that pre-1987 law was ultimately interpreted by a court subsequent to enactment of section 1277(c)(2)(D).* But one could

also construe it, as did the dissenting judge, to require determination of Petitioner's rights and obligations in terms of pre-1987 law *as it stood at the time of enactment of section 1277(c)(2)(D)*. That is, statutes that define rights and obligations in terms of the application of a pre-existing legal framework can be understood to refer to open-ended decisional rules that are subject to change *or* to refer to definite rules whose meanings, for constructional purposes, are fixed at the time of enactment of the new statute.

In this case, when Congress enacted section 1277(c)(2)(D), the only court decision construing the interplay between the relevant federal and Virgin Islands tax statutes was *Danbury I*. Congress, the BIR, and Petitioner were all fully aware of the existence of this decision; indeed, the whole point of section 1275(b) of the Tax Reform Act was to overrule it, and the whole point of section 1277(c)(2)(D) was to exempt Petitioner from its retroactive overruling. Accordingly, it is unnecessary in this case to consider how to construe statutes of this character when there are conflicting – or no – prior judicial interpretations. Rather, we are concerned only with cases in which the pre-enactment legal rules that bear on the interpretation of a statute are well understood. In such cases, we submit that Chief Judge Gibbons had it right and the majority had it wrong: statutes enacted against a well understood legal framework which define rights and obligations in terms of that framework should be *presumed* to incorporate the law as it stood at the time of enactment.

The reasons for such a presumption were aptly stated by Chief Judge Gibbons. If such statutes are deemed to

call for application only of pre-existing legal rules, parties will be able to determine their rights and obligations under these statutes from the moment of enactment. The powerful legal interest in certainty, which this Court has recognized in analogous contexts, *see* page 16, *infra*, is thereby served.

On the other hand, if the proper interpretation of a statute hinges on future, contingent judicial developments, parties must wait out – and litigate – the contingencies before knowing their rights. For example, the interpretation of section 1277(c)(2)(D) adopted by the Third Circuit in essence construed the statute to give Petitioner a roll of the judicial dice (or, more precisely, a stake in Danbury, Inc.,'s roll of the judicial dice), the outcome of which might not be known, given the possibility of Supreme Court review, for several years and several lawsuits. A more perverse reading of the statute would be difficult to imagine.

The reasons why such a presumption must be only a presumption rather than an absolute rule are the same as the reasons for so treating any canon of construction. One can imagine cases where it might be clear from the circumstances surrounding enactment of a statute that Congress precisely intended to commit the parties' rights and obligations to a roll of the judicial dice. Certainly, arguments to that effect should always be entertained, though it is not a remotely plausible claim in this case.[8]

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[8] We are not asking the Court to pass judgment on this assertion. Whether a presumption of the applicability of prior law can be overcome on the facts of this case is a question that could best be answered by the Court of Appeals on remand.

Nonetheless, whether one views the interest in certainty as a reflection of presumed congressional intent or of sound judicial policy, it is substantial enough to warrant a presumption against making statutory drafters and affected parties unwilling participants in a spin of the judicial "wheel of fortune".

B. This Court's Decisions Are Consistent With This Formulation of and the Rationale Behind Such a Presumption

This Court's decisions are consistent with both the formulation of and the rationale behind the interpretative presumption advanced here, though we are aware of no decision explicitly adopting (or rejecting) such a rule or addressing the issue in precisely the circumstances of the present case.

The most analogous authority is *Parker v. Motor Boat Sales, Inc.*, 314 U.S. 244 (1941). In *Parker*, the Court had to construe a proviso in the Longshoremen's and Harbor Workers' Act of 1927 (LHWA), ch. 509, 44 Stat. 1424 (codified at 33 U.S.C. § 919) limiting compensation to injured maritime employees under the Act to circumstances in which "recovery for the disability or death through workmen's compensation proceedings may not validly be provided by State law." 314 U.S. at 245. A prior, much criticized decision of the Court, *Southern Pacific Co. v. Jensen*, 244 U.S. 205 (1917), had held that the Constitution's grant of admiralty and maritime jurisdiction to the federal courts, *see* U.S. Const. art. III, § 2, cl. 1, automatically preempted any state laws interfering with "the harmony and uniformity of admiralty law." 314 U.S.

at 248. The Court held in *Parker* that, whatever the constitutional merits of the *Jensen* rule, the LHWA's proviso was enacted with that rule clearly in mind, and it accordingly exempted from the LHWA's coverage only those claims within the power of the states under *Jensen*. Significantly, the Court explicitly declared that its decision was independent of any future reconsideration of *Jensen*, citing the need for certainty in the determination of statutory rights:

> An interpretation which would enlarge or contract the effect of the proviso in accordance with whether this Court rejected or affirmed the constitutional basis of the *Jensen* and its companion cases cannot be acceptable. The result of such an interpretation would be to subject the scope of protection that Congress wished to provide, to uncertainties that Congress wished to avoid.

314 U.S. at 250. The Court thus accepted *Jensen* and its subsequent cases, without regard to their correctness, as "the measure by which Congress intended to mark the scope of the Act they brought into existence." *Ibid.* It did not, however, frame its decision in terms of a generalizable rule of construction, though its rationale is precisely congruent with the analysis put forward here.

Relying on *Parker*, the Court subsequently gave voice to the congressional policy of rejecting such uncertainty in the context of tax liability:

> Such an intention would be a serious departure from the usual policy of Congress to provide the taxpayers and tax gathers with a practical basis for the timely settlement of questions of taxation arising each year. . . .the government's assertion that Congress intended to hold the meaning of [the statute] in suspense until the termination of

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> years of litigation is in conflict with our recent decision in *Parker v. Motor Boat Sales, Inc.*

Helvering v. Griffiths, 318 U.S. 371 at 399 (1943).

More recently, the Court faced a somewhat related issue in *Brown v. GSA*, 425 U.S. 820 (1976). The question in the case was whether section 717 of the Civil Rights Act of 1964, 78 Stat. 253, 42 U.S.C. § 2000e-16 (1982), "provides the exclusive judicial remedy for claims of discrimination in federal employment." 425 U.S. at 821. Prior to 1972, when section 717 was made applicable to federal employees by the Equal Employment Opportunity Act of 1972, 86 Stat. 103 (codified at 42 U.S.C. § 2000e), there was considerable uncertainty concerning the scope of judicial and administrative remedies, if any, available to federal employees alleging racial discrimination. The Court surveyed the legislative history of the 1972 Act and found "little doubt that Congress was persuaded that federal employees who were treated discriminatorily had no effective judicial remedy." 425 U.S. at 828. Accordingly, the Court concluded "that the congressional intent in 1972 was to create an exclusive, pre-emptive administrative and judicial scheme for the redress of federal employment discrimination." *Id.* at 829. Whether Congress was justified in its belief that no remedies actually existed prior to 1972 was deemed to be of no consequence:

> Whether that understanding of Congress was in some ultimate sense incorrect is not what is important in determining the legislative intent in amending the 1964 Civil Rights Act to cover federal employees. For the relevant inquiry is not whether Congress correctly perceived the then state of the law, but rather what its perception of the state of the law was.

Id. at 828.

Brown is not strictly on point, because the statute at issue did not define rights and obligations in terms of prior law. Rather, *Brown* called only for application of the familiar and uncontroversial rule that one should construe a statute in light of the circumstances existing at the time of its enactment.[9] There is no reason, however, why the same principle should not govern interpretation of statutes that do not merely contemplate the existence of a prior legal framework, but explicitly call for its application to determine new rights. If Congress is presumed to know the state of prior law when it enacts statutes, it should similarly be presumed to incorporate those known rules when it makes explicit reference to prior law.

Thus, if *Brown*, *Helvering* and *Parker* can be generalized, they support the claim that a law defining rights and obligations in terms of the application of pre-existing legal rules should be presumed to call for application of those rules as they were understood to exist at the time of enactment, without regard to subsequent statutory or judicial changes. This case, however, is concededly unlike either *Parker* (which dealt with a prior *constitutional* interpretation) or *Helvering* and *Brown*, in that *Danbury I*, the

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[9] *See Cannon v. University of Chicago*, 441 U.S. 677, 711 (1979) (dictum). The application of that familiar rule can, of course, present difficult problems. In *Brown*, for example, Justice Stevens, joined by Justice Brennan, drew precisely the opposite inference than did the majority from Congress' 1972 assumption of no prior remedies: "The fact that Congress incorrectly assumed that federal employees would have no judicial remedy if § 717 had not been enacted undermines rather than supports the Court's conclusion that Congress intended to repeal or amend laws that it did not think applicable." 425 U.S. at 837-38 (Stevens, J., dissenting).

judicial decision constituting the relevant legal background, was on appeal when the Tax Reform Act was signed into law. This difference, though, should make no difference. The interests in certainty that in general support the presumption support it also in this circumstance; in the absence of the rule we propose, no one can know their rights under a statute like section 1277(c)(2)(D) until a full round of litigation has taken place. (Litigation may be necessary under our rule as well if the parties disagree about whether the presumption of incorporation of prior law can be overcome, but that is more easily ascertainable than a guess about the likely consequences of a post-enactment appeal.) Moreover, having a relevant judicial decision on appeal is no different in principle from having a relevant prior statute under reconsideration in the Congress or the Executive Branch. No one, we trust, would suggest in the latter case that we await the outcome of the legislative process before interpreting the new statute, unless Congress has ordered such a result in the clearest possible terms. Finally, if the fact of appeal is deemed relevant, there should at least be an exception for appeals to which the purported beneficiary of the new statute is not a party. In this case, the decision on appeal when section 1277(c)(2)(D) was enacted was *Danbury I*, and Petitioner was not a party to that case.

Thus, as matters developed, Bizcap's rights were essentially made contingent on the outcome of an appeal in which it was not a participant.[10]

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[10] This circumstance is a by-product of the Third Circuit's misinterpretation of its own prior opinion, for which we are

(Continued on following page)

CONCLUSION

In sum, we ask the Court explicitly to declare that statutes which determine rights and obligations by reference to pre-existing legal rules presumptively call for application of those rules as they stood at the time of enactment, and that this presumption is not affected by the fact that one or more of the relevant rules are on appeal. On the facts of this case, that will leave only the question of whether this presumption can be overcome, and we will be happy to cross arms with the Respondents on that issue in the Court of Appeals, under proper legal instructions.

Respectfully submitted,

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(Continued from previous page)

not seeking relief in this Court. When *Danbury II* was decided, Danbury's attempt to claim a tax benefit had been settled by section 1275(b) of the Tax Reform Act; there was no occasion for the Court of Appeals to address any of the issues that had been litigated in *Danbury I*. Nonetheless, it did so, and the Court of Appeals in this case simply adopted the dicta of *Danbury II* as a holding. However, given the Court of Appeals' interpretation of section 1277(c)(2)(D) in this case, it would still have had to express a view on the correct interpretation of pre-Tax Reform Act law as to the inhabitant rule. Thus, we do not place great weight on our lack of party status in *Danbury II*.

Filed: December 29, 1989

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 89-3199

BIZCAP, INC.

Appellee

vs.

ANTHONY P. OLIVE, Director of Virgin Islands Bureau of Internal Revenue, and the GOVERNMENT OF THE VIRGIN ISLANDS

Appellants

Appeal from the District Court
of the Virgin Islands
(Division of St. Croix)
(Civil No. 86-18)

Argued
December 6, 1989
Before: GIBBONS, *Chief Judge.*
MANSMANN and NYGAARD,
Circuit Judges.

(Filed December 29, 1989)

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OPINION OF THE COURT

MANSMANN, *Circuit Judge.*

We are faced here with the confusion which results when an erroneously decided opinion is legislatively corrected prior to its ultimate reversal by the court of appeals. Thus, we must decide whether a Virgin Islands corporation, which lobbied for an exception to the Tax Reform Act of 1986, won a hollow victory and found itself, though not liable to the United States Internal

Revenue Service for tax on its stateside income, nevertheless liable to the Virgin Islands Bureau of Internal Revenue. We conclude that the exception in § 1277(c)(2)(D) of the Tax Reform Act of 1986 exempts Bizcap, Inc., from the retroactive effect of the Act with respect to pre-1987 open years. However, the result is to hold Bizcap liable to the BIR for the pre-1987 tax years for which the BIR filed a deficiency notice within the statute of limitations. Since the district court entered summary judgment for Bizcap and found that Bizcap was not liable for any deficiency, either to the IRS or the BIR, we will reverse the decision of the district court.

I.

Caribbean Marine, Inc., a/k/a/ Bizcap, Inc., a Delaware corporation since March 31, 1983, is considered an inhabitant of the Virgin Islands for purposes of § 28(a) of the Revised Organic Act, Act of July 22, 1954, c. 558, § 28(a), 68 Stat. 508, *codified at* 48 U.S.C.A. § 1642 (West 1987).[1] Bizcap filed United States income tax returns of a foreign corporation with the Bureau of Internal Revenue in the Virgin Islands ("BIR") for Bizcap's tax years ending May 1983 and 1984. Bizcap filed no forms with the U.S. Internal Revenue Service ("IRS") for the same tax years.

Bizcap's 1982 1120F Form (foreign corporation) for 1983 listed non-Virgin Islands source income of over $ 15 million, and its 1983 1120F Form for 1984 listed non-

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[1] The Revised Organic Act, passed in 1954, provides the basic charter for the civil government of the people of the Virgin Islands.

Virgin Islands source income of $ 1.6 million. Bizcap's 1982 1120F for Virgin Islands source income listed a loss of $ 36,052, while the 1983 1120F Form listed Bizcap's Virgin Islands source income as $ 18,979. Consequently, Bizcap paid $ 157 in income tax to the BIR on the Virgin Islands source income. Bizcap paid no tax to the IRS on its $ 16.9 million income from stateside sources.

On November 7, 1985, the BIR issued a deficiency notice to Bizcap, determining that Bizcap owed $4,467,439 in tax and $ 670,116 in penalty for 1983 as well as $ 650,319 in tax and $ 97,548 in penalty for 1984. Bizcap filed a petition for redetermination of tax liability in the District Court of the Virgin Islands.

On October 22, 1986, Congress passed the 1986 Tax Reform Act which included a section granting an exception from IRS taxation to two Virgin Islands inhabitant corporations, one of which is Bizcap. On November 10, 1986, Bizcap filed a motion for summary judgment claiming it owed no taxes in light of the exception in § 1277(c)(2)(D) of the Tax Reform Act. The district court issued a memorandum and order granting judgment to Bizcap and concluding that Bizcap owed no tax deficiencies for the years 1983 and 1984. The Director of the BIR appeals, contending that, while Bizcap does not owe taxes to the IRS, it nevertheless owes them to the BIR.

II.

While the facts of this appeal are relatively straightforward, the issues can become complex unless the evolution of Virgin Islands tax law is set forth. After the Virgin Islands were ceded to the United States by Denmark in

1917, Congress passed the Act of March 3, 1917, ch. 171, § 4, 39 Stat. 1133, which continued in effect all of the local laws imposing taxes until Congress provided otherwise. In 1921, as part of the Naval Appropriations Act of 1921, Congress passed a statute which created a separate taxing structure mirroring the provisions of the federal tax code. Act of July 12, 1921, c. 44, § 1, 42 Stat. 123, [as amended, found at 48 U.S.C.A. § 1397 (West 1987)]. The result of the passage of the legislation was to substitute "Virgin Islands" for "United States" in the Internal Revenue Code, 26 U.S.C. § 1 *et seq.* Thus, to satisfy its obligations to the Virgin Islands, an individual or corporation pays the same amount of taxes to the BIR as it would pay under the same situation in the United States to the IRS. However, until 1935, the IRS and the United States Treasury treated the Virgin Islands as a collection district for United States taxes, rather than recognizing the distinct tax jurisdiction of the Virgin Islands. *See Danbury, Inc. v. Olive*, 820 F.2d 618 (3d Cir. 1987). "Under the collection district approach, all taxpayers with attachments to both locations filed only one return, either in the Virgin Islands or the United States, depending upon where the taxpayer resided on the last day of the tax year." *Danbury*, 820 F.2d at 621.

After 1935, when the mirror tax system was actually implemented, some individuals had to file two returns. For example, a United States corporation doing business in the Virgin islands would have to file a return with the IRS declaring its tax on stateside or world wide income as well as file a return with the BIR on its Virgin Island source income. *Id.* The passage of § 28(a) of the 1954

Revised Organic Act of the Virgin Islands changed the law again. Section 28(a) provides in pertinent part:

> The proceeds of customs duties, the proceeds of the United States income tax, the proceeds of any taxes levied by the Congress on the inhabitants of the Virgin Islands. . . .shall be covered into the treasury of the Virgin Islands, and shall be available for expenditure as the Legislature of the Virgin Islands may provide: *Provided* that the terms "inhabitants of the Virgin Islands" as used in this section shall include all persons whose permanent residence is in the Virgin Islands, and such persons shall satisfy their income tax obligations under applicable statutes of the United States by paying their tax on income derived from *all* sources both within and outside the Virgin Islands into the treasury of the Virgin Islands.

Act of July 22, 1954, c. 558, § 28(a), 68 Stat. 508, *codified at* 48 U.S.C.A. § 1642 (West 1987) (emphasis added). In addition, Congress enacted 26 U.S.C. § 7651(5)(B) of the Internal Revenue Code which stated that "For the purposes of this title . . . section 28(a) of the Revised Organic Act of the Virgin Islands shall be effective as if such section had been enacted subsequent to the enactment of this title." 26 U.S.C.A. § 7651(5)(b) (West 1967). Section 28(a), which came to be known as the "inhabitant rule," eliminated the need for an individual to file two returns. Instead, an inhabitant of the Virgin Islands could file one form and report all income earned, both Virgin Islands and worldwide sources, to the BIR and pay taxes to the BIR.

On January 24, 1986, the district court for the Virgin Islands issued a decision in *Danbury, Inc. v. Olive*, 627 F.

Supp. 513 (D.V.I. 1986) which created a tax loophole. The district court reasoned, albeit erroneously, as follows. Danbury considered itself both a foreign corporation and an inhabitant of the Virgin Islands. Section 882 of the Internal Revenue Code states that a non-inhabitant foreign corporation is liable only for taxes on income derived from a trade or business connected with the Virgin Islands. As a general rule, income that a foreign corporation derives from stateside or worldwide income cannot be taxed by the Virgin Islands. 26 U.S.C. § 882. Thus, the district court concluded, as a foreign corporation, Danbury could not be taxed by the BIR on stateside income. Since Danbury was an inhabitant of the Virgin Islands, it was to pay its taxes to the BIR and not to the IRS. Consequently, the district court reasoned, Danbury had to pay only the taxes due on its Virgin Islands source income and the income from stateside business was exempt.

The creation of the tax loophole by the district court in *Danbury* was rectified in two ways. First, the BIR appealed to us, and second, changes were made to the mirror code system in the Tax Reform Act of 1986. Pub. L. No. 99-514, 100 Stat. 2085. Because the Tax Reform Act occurred before we reviewed *Danbury*, we will discuss it first. The Act contains a provision entitled "Clarification of Treatment of the Virgin Islands Inhabitants" found at § 1275(b) which amends 26 U.S.C. § 7651(5)(B) to read:

> For purposes of this title, section 28(a) of the Revised Organic Act of the Virgin Islands shall be effective as if such section 28(a) had been enacted before the enactment of this title and such section 28(a)

> shall have no effect on the amount of income tax liability required to be paid by any person to the United States.

26 U.S.C.A. § 7651(5)(B) (West Supp. 1987). As a result of § 1275(b), the Virgin Islands tax system returned to the pre-1954 system where a foreign corporation doing business in the Virgin Islands must file two returns; one return to the IRS for its stateside income and one to the BIR for Virgin Islands source income.

Section 1277(c)(2) of the Act outlined the date of implementation of the Act.

> (A) In General. – The amendment made by section 1275(b) shall apply with respect to–
>
> (i) any taxable year beginning after December 31, 1986 and
>
> (ii) any pre-1987 open year.
>
> * * *
>
> (C) Pre-1987 Open Year. – For purposes of this paragraph, the term "pre-1987 open year" means any taxable year beginning before January 1, 1987, if on the date of the enactment of this Act the assessment of a deficiency of income tax for such taxable year is not barred by any law or rule of law. Tax Reform Act of 1986, Pub. L. No. 99-514, Title XII, § 1277(c)(2), *reprinted at note* 26 U.S.C.A. § 931 (West 1988).

Following the enactment of the Tax Reform Act, we decided *Danbury, Inc. v. Olive*, 820 F.2d 618 (3d Cir. 1987) and reversed the district court. We determined that the inhabitant rule required that a stateside corporation otherwise considered an inhabitant of the Virgin Islands be held liable to the BIR for tax on all income, and pursuant

to the new tax law, Danbury could be found liable to the IRS and the BIR if the district court determined that the years in question were pre-1987 open years. For the purposes of Bizcap, the holding in *Danbury*, 820 F.2d 618, eliminated the judicially created loophole.

III.

We turn now to the specific issue presented by this appeal. Our review of the granting of a motion for summary judgment requires us to apply the same standard as applied by the district court. *See Koshatka v. Philadelphia Newspapers, Inc.*, 762 F.2d 329 (3d Cir. 1985). Thus, we must determine that there exists no genuine issue as to material fact and that the moving party is entitled to judgment as a matter of law. Fed. R. Civ. Pro. 56. Because the only issues here involve the interpretation of a targeted exception to the retroactive effect of the Tax Reform Act of 1986, we can make the determination as a matter of law.

Bizcap claims that it owes no taxes on stateside income for the tax years ending May, 1983, and 1984, because it falls within the exception provided in § 1277(c)(2)(D) of the Tax Reform Act. That provision states:

> (D) Exception. – In the case of any pre-1987 open year, the amendment made by section 1275(b) shall not apply to any domestic corporation if –
>
> (i) during the fiscal year which ended May 31, 1986, such corporation was actively engaged directly or through a subsidiary in the conduct of a trade or business in the Virgin Islands and

such trade or business consists of business related to marine activities, and

(ii) such corporation was incorporated on March 31, 1983, in Delaware.

Pub.L. No. 99-514, Title XII, § 1277, 100 Stat. 2593, *reprinted at note* 26 U.S.C.A. § 931. Bizcap contends that the targeted exception contained in § 1277(c)(2)(D) was intended to grant Bizcap an exception from both IRS and BIR taxation on its non-Virgin Island source income.

Neither Bizcap nor the BIR dispute that the exception in § 1277(c)(2)(D) was intended for Bizcap [a/k/a/ Caribbean Marine, Inc.]. The BIR, however, claims that the exception exempts Bizcap from IRS liability, but not from tax liability to the BIR. We agree. Section 1277(c)(2)(D) effectively treats Bizcap as though the Tax Reform Act of 1986 had never been enacted for those years which are pre-1987 open years. A pre-1987 open year is one in which the statute of limitations has not run against either the BIR or the IRS. While the IRS failed to file a deficiency notice with Bizcap on Bizcap's stateside income,[2] the BIR did file a deficiency notice for both 1983 and 1984. Therefore, 1983 and 1984 are pre-1987 open years with respect to the BIR. Since 1983 and 1984 are open years, § 1277(c)(2)(D) provides that § 1275(b) of the Tax Reform Act – the section repealing the inhabitant rule – does not apply to Bizcap.

At the time the Act was passed, Congress believed the interplay between 26 U.S.C. § 882 and § 28(a) resulted

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[2] This was not a mistake on the part of the IRS which naturally assumed that Bizcap would pay all its taxes to the Virgin Islands pursuant to the inhabitant rule. § 28(a).

in a tax loophole. Bizcap lobbied to have the loophole applied to it by avoiding the retroactive effect of the repeal of the inhabitant rule. However, since we determined in *Danbury*, 820 F.2d at 625, that there was no loophole, the exception granted to Bizcap results in Bizcap remaining liable to the BIR for taxes on both its stateside and Virgin Islands source income for 1983 and 1984.

Bizcap argues, and the dissent agrees, that Congress intended for Bizcap to have a complete exemption from tax liability on its stateside income. However, the plain language of the exception only exempts Bizcap from the retroactive effect of the tax law change. Thus, Bizcap remained liable under the previous tax laws applicable to the Virgin Islands, whatever they were or were determined to be by our court in *Danbury*.[3] Bizcap and its lobbyists were fully aware that the *Danbury* decision had been appealed to us and that the decision could be reversed. Rather than couch the exception in terms of the retroactivity of the repeal of the inhabitant rule, the drafters of the legislation could have specifically stated that the targeted corporations were exempt from tax liability on stateside income for the years in question. However, that is not what happened here. Instead, Congress chose clear language which linked Bizcap's exception to the

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[3] Indeed, as explained in the history of the Tax Reform Act, under present law: "An 'inhabitant' of the Virgin Islands pays tax to the Virgin Islands on its worldwide income, but pays no U.S. tax." H. Conf. Rep. 99-841, Title XII, II-679, *reprinted at*, 1986 U.S. Code Cong. & Admin. News. 4075, 4767 (1987).

application of the Virgin Islands law prior to the repeal of the inhabitant rule. We are not at liberty to ignore the plain language of a congressional enactment. *See Central Trust Co. v. Creditor's Committee*, 454 U.S. 354, 360 (1982) (per curiam), *citing*, *Caminetti v. United States*, 242 U.S. 470, 485 (1917) ("It is elementary that the meaning of a statute must, in the first instance be sought in the language in which the act is framed, and if that is plain, and if the law is within the constitutional authority of the law-making body which passed it, the sole function of the courts is to enforce it according to its terms.").

Bizcap asks us to ignore our decision in *Danbury* and support its exemption on the basis of congressional intent as evidenced by the legislative history. We acknowledge that Bizcap was obviously intended to be excepted from the retroactive effect of the repeal of the inhabitant rule.[4] It was our reversal of the district court's decision in *Danbury*, where we stated that no loophole *ever existed*, which effectively eliminated the loophole for Bizcap. Indeed, in its trial brief, the BIR admitted that had we not

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[4] The dissent misconstrues our reasoning and concludes that we imply "Congress intended to make the effect of the statute depend on our subsequent determination in *Danbury* of the scope of section 1275(b) and the inhabitant rule." We have merely recognized that Congress intended to grant Bizcap an exemption from the repeal of the inhabitant rule. Had we affirmed the district court's opinion in *Danbury*, Bizcap would not be liable to either the BIR or the IRS for taxes. However, such was not the case. The result, Bizcap's liability, is totally separate from the mechanics of the repeal of the inhabitant rule. Bizcap's liability stems from the fact that the BIR had filed deficiency notices for the tax years ending May, 1983 and 1984 thereby keeping those years open with respect to the BIR.

reversed the district court's decision in *Danbury*, Bizcap would not owe any taxes on its stateside income. But we are not free to ignore the holding of another panel of this court absent reversal of the opinion after consideration by the entire court. I.O.P. Chapter 8 (C). Thus, we must apply the exception in § 1277(c)(2)(D) in light of our holding in *Danbury*.

IV.

Because we conclude that the effect of § 1277(c)(2)(D) was to except Bizcap from the retroactive effect of the repeal of the inhabitant rule, thereby leaving Bizcap in the position it would have been had the Tax Reform Act of 1986 not been enacted, Bizcap remains liable to the BIR for those pre-1987 years for which the BIR filed deficiency notices. Consequently, we will reverse the decision of the district court which entered judgment for Bizcap and remand for a determination of liabilities, penalties and interest due the BIR.

GIBBONS, *Chief Judge*, dissenting.

The Court's depiction of the evolution of Virgin Islands tax law and of the problem which faces us here is accurate enough, but the solution it adopts is highly technical and flies in the face of common sense.

The problem is indeed one of statutory interpretation. As a general matter the Court is correct and in accord with hoary precedent when it writes, "We are not at liberty to ignore the plain language of a congressional enactment." Slip Op., typescript at 12. However, the actual English words of the statue we are to interpret are:

statute

> (D) *Exception.* – In the case of any pre-1987 open year, the amendment made by section 1275(b) shall not apply to any domestic corporation if –
>
> (i) during the fiscal year which ended May 31, 1986, such corporation was actively engaged directly or through a subsidiary in the conduct of a trade or business in the Virgin Islands and such trade or business consists of business related to marine activities, and
>
> (ii) such corporation was incorporated on March 31, 1983, in Delaware.

Tax Reform Act of 1986, Pub. L. No. 99-514, § 1277(c)(2)(D), 100 Stat. 2085, 2601, (reprinted as note after 26 U.S.C.A. § 931 (West Supp. 1989)). Surely, this language is "plain" in some ways and not in others. It is plain that this enactment functions to exempt Bizcap, the corporation described here, from the effects of section 1275(b) for the period specified – whatever those effects may have been. The effects of section 1275(b), however are not "plain" from these words; they can be discerned only in the section's own words:

> (b) *Clarification of Treatment of Virgin Islands Inhabitants.* – Subparagraph (B) of section 7651(5) (relating to the Virgin Islands) is amended to read as follows:
>
> "(B) For purposes of this title [ie., U.S.C. tit. 26, the Internal Revenue Code], section 28(a) of the Revised Organic Act of the Virgin Islands shall be effective as if such section 28(a) had been enacted before the enactment of this title and such section 28(a) shall have no effect on the amount of income tax liability required to be paid by any person to the United States."

Tax Reform Act of 1986, Pub. L. No. 99-514, § 1275(b), 100 Stat. 2085, 2598 (amending Internal Revenue Code of 1954, § 7651(5)(B), 26 U.S.C. § 7651(5)(B) (1976)). When this Court interpreted section 1275(b) in *Danbury, Inc. v. Olive*, 820 F.2d 618 (3d Cir. 1987), we treated the language as "plain" in the sense that we did not reach beyond the statutory text itself in order to construe it. We found that the statute "repeals the 'inhabitant rule' . . . the rule that inhabitants of the Virgin Islands satisfy tax obligations to the United States by paying those taxes to the Virgin Islands rather than to the Internal Revenue Service." *Id.* at 625. But the precise effects of the inhabitant rule, in turn, are not themselves "plain" from the language of this statute.

The inhabitant rule stems from yet another statute, section 28(a) of the Revised Organic Act of 1954, ch. 558, 68 Stat. 497, 508 (codified as amended at 48 U.S.C. § 1642 (1982)). In *Danbury* we did find that section 28(a) was itself "unambiguous," *Danbury* at 622, but nonetheless the rule which stemmed from it had had several effects in the real world. One effect was that all taxes paid by residents of the Virgin Islands went into the Virgin Islands treasury, even if the taxpayer was a foreign corporation. Another effect, which obtained until our decision, was that the taxes some foreign corporations paid included no taxes at all on non-Virgin Islands income. This second effect was a mistaken application of section 28(a), as we held in *Danbury*, but the mistake is plain only upon examination of section 28(a) itself.

There are thus three statutes to interpret in this case, and the language of each is plain in a different way. The clear purpose of Congress in enacting section 1275(b) –

and this is what is "plain" in its language – was to erase all the effects of the inhabitant rule. One perceived effect was exemption from all non-Virgin Islands taxation. In the majority's own words, "Congress believed the interplay between 26 U.S.C. § 882 and § 28(a) resulted in a tax loophole." Slip op., typescript at 11. Congress therefore designed to collect taxes on U.S.-source income from all Virgin Islands inhabitants and to deposit the proceeds in the federal treasury. It seems plain to me, therefore, that the purpose of section 1277(c)(2)(D) was both to direct to the BIR whatever taxes Bizcap was liable for, and also to exempt it from taxes on its non-Virgin Islands income. The majority's approach seems rigid and technical, and the artificial consistency it imposes on the interpretation of the three statutes distorts the plain language of section 1277(c)(2)(D).

Technically, I suppose, the purpose of Congress evident on the face of section 1277(c)(2)(D) could have been either to grant Bizcap a complete exemption from taxation for a few pre-1987 years, or to give the Virgin Islands a few more years of tax revenue from Bizcap. But it is hard to imagine that when Congress identified Bizcap as a targeted exception to the retroactive application of the repeal of the inhabitant rule, it intended to benefit the Virgin Islands. The point of singling out Bizcap was to benefit Bizcap. And of course the extrinsic evidence of congressional intent, as the district court pointed out, is unequivocal: the legislative history of section 1275(b) shows clearly that Congress thought it was closing a loophole allowing exemption from all taxation on non-

Virgin Islands income; Bizcap lobbied hard for its exception in section 1277(c)(2)(D); and the BIR lobbied hard against it.

The logic of the majority opinion is to impute yet another intent to Congress in enacting section 1277(c)(2)(D), one I find more unlikely still. The majority implies that Congress intended to make the effect of the statute depend on our subsequent determination in *Danbury* of the scope of section 1275(b) and the inhabitant rule. That analysis suggests that, since the lobbyists knew the appeal was pending and the legislature rejected alternative language for the targeted exception, the statute's purpose was merely to make Bizcap's fortunes depend on Danbury's success in the Court of Appeals, as we later construed another statute, in litigation in which Bizcap was unrepresented. That is, the majority would now have us believe that the purpose of Congress evident on the face of section 1277(d)(2)(D) was not to hand Bizcap a victory, nor even to hand the BIR a victory, but to give Bizcap a sporting chance of victory in the *Danbury* court. This logically awkward conclusion strains credulity. I would affirm.

A True Copy:

Teste:

Clerk of the United States Court
of Appeals for the Third Circuit

IN THE DISTRICT COURT OF THE VIRGIN ISLANDS
DIVISION OF ST. THOMAS AND ST. JOHN

CARIBBEAN MARINE, INC., (FORMERLY KNOWN AS BIZCAP, INC.),	)	
Petitioner,	)	CIVIL NO. 1986-18
vs.	)	
ANTHONY P. OLIVE, Director of Bureau of Internal Revenue, and GOVERNMENT OF THE VIRGIN ISLANDS,	)	
Respondents,	)	

ORDER

An opinion of even date herewith having been filed, it is hereby *ORDERED and ADJUDGED* that consistent with said opinion no deficiency in taxes exist as to Caribbean Marine, Inc. for the years 1983 and 1984.

DATED this 23rd day of February, 1989.

ENTER:

/s/ David V. O'Brien
DAVID V. O'BRIEN
Chief Judge

ATTEST: Orinn Arnold
Clerk

by: /s/ _____
Deputy Clerk

IN THE DISTRICT COURT OF THE VIRGIN ISLANDS
DIVISION OF ST. THOMAS & ST. JOHN

CARIBBEAN MARINE, INC., (FORMERLY KNOWN AS BIZCAP, INC.),	)	
Petitioner,	)	CIVIL NO. 1986-18
vs.	)	
ANTHONY P. OLIVE, Director of Bureau of Internal Revenue, and GOVERNMENT OF THE VIRGIN ISLANDS,	)	
Respondents,	)	

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O'BRIEN, Chief Judge

MEMORANDUM OPINION

This case arises out of the opinion issued by this Court in *Danbury v. Olive*, 627 F. Supp. 513 (D.V.I. 1986)

which had a brief life until overruled by the Third Circuit at 820 F.2d 618 (3d Cir. 1987). While this Court's decision was still in force, the events involved herein arose. At issue is whether the Government of the Virgin Islands may collect several million dollars from the petitioner Caribbean Marine, Inc. (CMI) in the face of Congressional action which CMI claims provides relief from such a claim. We hold that the petitioner is exempt from Virgin Islands taxation for the years in question as a result of the targeted exception granted by Congress.

I. FACTS

When we decided *Danbury, supra,* we held that corporations organized in the United States which were inhabitants of the Virgin Islands were exempt from taxation by the Virgin Islands on income derived from outside the Virgin Islands. In so ruling we interpreted the Revised Organic Act of the Virgin Islands, § 28(a), 48 U.S.C.A. §1642.

This loophole was being utilized by hundreds of stateside corporations with hundreds of millions of dollars of assets. Millions of dollars in potential taxes were at stake. One of these corporations was the petitioner CMI. There was one difference, however, between CMI, and most of the other corporations. [CMI] conducted extensive business in the Virgin Islands as well as on the mainland, and it had a significant payroll in the territory.

After our opinion was issued in January, 1986 and before the Third Circuit dissected and discarded our holding, taxing authorities rushed to Congress to vitiate

the effects of the decision. The effort involved retroactively repealing the "inhabitant rule" contained in Section 28(a) of the Revised Organic Act. If successful, the loophole would be closed.

CMI had been served with a Notice of Deficiency by the Bureau of Internal Revenue of the Virgin Islands for the years 1983 and 1984. The territorial government claimed that CMI owed taxes, penalties and interest to the Virgin Islands on its non-Virgin Islands source income. For the tax year ended 1983, the territory claimed $4,467,439 in a tax deficiency and $670,116 as a penalty. For the 1984 tax year, it claimed $650,319 in taxes and $97,548 as a penalty, for a total then calculated at $5,885,422. Upon receipt of the Notice, CMI filed this action. CMI also took steps to obtain a "targeted exception" to any action of Congress which would put it in the position of paying taxes.

Its efforts were successful. Together with another corporation in a similar situation, a "targeted exception" was granted in the Tax Reform Act of 1986, §1277(c) which reads:

> (D) Exception. – In the case of any pre-1987 open year, the amendment made by section 1275(b) shall not apply to any domestic corporation if –
>
> (i) during the fiscal year which ended May 31, 1986 such corporation was engaged directly or through a subsidiary in the conduct of a trade or business in the Virgin Islands and such trade or business consists of business related to marine activities, and

(ii) such corporation was incorporated on March 31, 1983 in Delaware.

Armed with that legislation, CMI argued to the territorial government that it was not liable for any taxes. The territorial authorities, on the other hand, held that while CMI may have escaped liability for federal taxes, the legislation in question did not exempt the corporation from its territorial tax responsibilities, for 1983 and 1984.

The local government makes two arguments in this case: (1) the legislation itself was not intended to exempt CMI from Virgin Islands taxes and (2) even if it was so intended, the phrase "pre-1987 open years" in the targeted exception only exempted the corporation from taxation for one of the two years in question, i.e. 1984.

There is also the issue whether the Third Circuit's decision reversing us has any effect on the outcome. The territorial government claims that the reversal reinforces its argument that CMI is not exempt, while CMI argues that the holding is "superfluous" and mere "dicta", since it was entirely based on the provisions of the Tax Reform Act and its retroactive repeal of the inhabitant rule. CMI claims the Third Circuit never even considered the targeted exception. We now take up these issues.

II. DISCUSSION

A. Congressional Intent

Did Congress intend to exempt CMI from both federal and local taxation in its passage of the targeted exception? That is the central question posed in this case. When CMI became aware that the U.S. Treasury Department

was attempting to have the inhabitant rule revoked as a method to offset our original *Danbury* decision, it moved quickly to seek a targeted exception. CMI claims that the local government fought vigorously against its attempts, to the extent that it hired Washington, D.C. lawyer/lobbyists to overcome the CMI position. Peter Hiebert, Esq. was one of the lawyer/lobbyists retained by the territorial government to achieve the local government's goal. When the issue of the involvement of Mr. Hiebert was raised repeatedly by CMI in the discovery process and in argument to this Court, the normally concise articulation of the territorial government's counsel descended into obfuscation. When CMI described the Hiebert activity through affidavits of persons who dealt with him personally, the local government did not produce any countervailing affidavit from Mr. Hiebert. What the local government did do is attempt to dissimulate about his involvement on its behalf. No amount of dissimulation, however, can overcome the effectiveness of the CMI affidavits describing the local government's posture concerning the targeted exception.

The activity of the local government in response to the CMI efforts is important to us for one simple reason: if the local government opposed the targeted exception, it lends strength to the CMI argument that the territory knew all along what the purpose of the legislation was. Further, that the territory knew that its successful passage would result in the exemption of CMI from local taxation for the years in question. The local government would have no other logical reason to act in such a fashion, except if a loss of revenue was involved.

The territory argues that the language of the targeted exception quoted above does not result in exemption from anything more than federal taxation. When faced with legislative language, courts proceed carefully in the interpretation of such wording. We look at the timing of the legislation and the existing law being amended or changed in some fashion. At the time the targeted exception was being sought to offset the revocation of the inhabitant rule, this Court's decision in *Danbury* was the only law on the subject. We had held that companies such as CMI owed no tax on their non-Virgin Islands source income. The Treasury Department was seeking to obviate that decision and CMI was seeking to overcome the Treasury Department's and the local government's effort by means of the targeted exception. For the territorial government to argue, as it does in this case, that all Congress intended was to actually provide for local taxation of CMI's income during the years in question strains our sense of logic. Why would there be this frenetic activity simply to shift the place where the taxes were to be paid? Under such reasoning, why would the local government fight the targeted exception if under such a view it would obtain substantial tax income?

Likewise, if Congress intended merely to shift the locale where the taxes were to be paid, would it not have so stated in its report on the revenue effect of the targeted exception? The Joint Committee on Taxation described the effects of the two targeted exceptions being considered, one of which was CMI, as follows:

"Revenue Effect

The provision is estimated to decrease fiscal year budget receipts by $14 million in 1987 and

> to have a negligible effect on budget receipts thereafter."

CCH Vol.74, No.19, May 8, 1987 at 1127.

Congressional intent can be manifest by what is not stated as well as by what is said. *Watt v. Alaska*, 451 U.S. 266-67 (1981); *Charles v. Charles*, 788 F.2d 960, 966 (3d Cir. 1986); *United States v. Perdue Farms, Inc.*, 680 F.2d 277, 283-84 (2d Cir. 1982). In this case, if it were the intent to shift the taxing right to the Government of the Virgin Islands, surely the explanation would have covered that result, by noting that the revenue loss was not total, but rather, the Virgin Islands would benefit from its ability to tax the two targeted exceptions by the same amount as the federal decrease.

The action by the Third Circuit in reversing this Court's holding in the original *Danbury* decision does not affect the act of Congress in granting a targeted exception to CMI. The Third Circuit did not discuss the matter in the framework of the targeted exception of CMI. It discussed the Tax Reform Act and the revocation of the inhabitant rule and then defined what "pre-1987 open years" would mean to Danbury, a corporation covered by the revocation of the inhabitant rule and not the beneficiary of any targeted exception. Certainly the Circuit Court cannot be held to have ruled concerning CMI and its targeted exception when reversing Danbury. It did not have that issue before it. The Circuit Court decision in *Danbury* is controlling as to like corporations not granted a targeted exception, but where Congress has legislatively exempted a corporation from federal and local taxes for certain years, one can never contemplate that

the Third Circuit would overcome the act of a separate branch of government and reinstate the taxes.

The territory argues further, however, that the Third Circuit ruling in *Danbury* did fix what is meant by pre-1987 open years, and that under such a ruling, CMI must still lose the exemption for 1983, the year when the greatest amount is sought under the deficiency notice.

We find that the congressional intent is clear, i.e., that CMI was to be excepted from the retroactive revocation of the inhabitant rule, and exempt from any federal or local taxes for the years 1983 and 1984. We discuss below the contention of the local government as to what constitutes a pre-1987 open year.

B. What Is A Pre-1987 Open Year?

The territory argues that even if Congress intended to exempt CMI from Virgin Islands taxes, it only did so for what could be described as "pre-1987 open years". That language, as cited earlier in this opinion, is indeed contained in the targeted exception. The Third Circuit defined a pre-1987 open year as a year when the federal government could still exercise its jurisdiction to seek a deficiency, when it decided *Danbury*, 820 F.2d at 626. Therefore, according to the territory, since the territory was not included in the definition, it could exercise its jurisdiction as to any such years in which it could still seek deficiencies.

The Third Circuit, however, was not dealing with what Congress meant in its targeted exception, but only with corporations such as Danbury for whom elimination

of the inhabitant rule left it open to taxation by the federal government in any pre-1987 open years. Congress did not grant exceptions to such corporations except CMI and one other. If its intent was to exempt the corporations covered by the targeted exception from both federal and local taxes, it follows then, that the definition of what constitutes a pre-1987 open year, as to the targeted exceptions, would include those still available to both taxing jurisdictions to seek tax deficiencies. To read such a definition otherwise as to the targeted exceptions would be to thwart the will of Congress as we have construed it.

The territory also makes an argument which concedes that under the Third Circuit holding in *Danbury*, 1984 is a pre-1987 open year for federal purposes, and thus cannot exercise its own tax jurisdiction. But, it asserts, since 1983 is not such a year for the federal government, it is such a year for the local government. In view of the fact that we find that the definition of pre-1987 open year applies to the right of both the federal government and the territorial government to seek a deficiency, we need not discuss that contention at any length.

In sum, as to the issue of what constitutes a pre-1987 open year, we interpret the congressional language in the only manner consistent with congressional intent, and that is to apply the phrase to both federal and local government, thus preserving the exemption of CMI from taxes to both governments for 1983 and 1984.

III. CONCLUSION

We find that Congress intended to grant an exemption to CMI from both federal and local taxes for 1983 and

1984, which might have resulted from revocation of the inhabitant rule. We further find that, consistent with that intent, a pre-1987 open year is any year in which either the federal or local government was capable of seeking a tax deficiency from CMI. Judgment will enter in favor of CMI declaring that no deficiency in taxes exists for the tax years in question to the Government of the Virgin Islands.

DATED this 23rd day of February, 1989.

/s/ David V. O'Brien